



The Commonwealth of Massachusetts

DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

December 6, 2004

D.T.E. 04-115

REQUEST FOR COMMENTS ON THE PROCUREMENT OF DEFAULT SERVICE POWER SUPPLY FOR RESIDENTIAL AND SMALL COMMERCIAL AND INDUSTRIAL CUSTOMERS

I. INTRODUCTION

On February 28, 2005, the seven-year transition period established by the 1997 Electric Restructuring Act will come to a close. All remaining standard offer service¹ customers will become default service customers on March 1, 2005. Despite the Department of Telecommunications and Energy's ("Department") best efforts to remove barriers to the development of an active retail competitive market for all customers,² most of the electricity consumed by residential and small commercial and industrial customers ("C&I") currently is provided through standard offer service and default service. Beginning March 1, 2005,

¹ Standard offer service has been provided at rates that ensure customers realize a 15 percent reduction in monthly electric bills, compared to bills from August 1997. The 15 percent reduction is adjusted for inflation and fuel costs.

² The Department has undertaken several comprehensive investigations designed to remove barriers to retail competition. See e.g., Pricing and Procurement of Default Service, D.T.E. 99-60 (1999); Metering and Billing, D.T.E. 01-28 (2001); Competitive Market Initiatives, D.T.E. 01-54 (2001); Provision of Default Service, D.T.E. 02-40 (2002).

approximately 95 percent of residential electricity consumption and 90 percent of small C&I electricity consumption will be provided through default service.³

The Department remains committed to maintaining and improving a sound framework for a competitive retail market for all customers. See Provision of Default Service, D.T.E. 02-04-B at 7 (2002). We note, however, that the competitive market serving low-use, low-load-factor customers has lagged. In addition, we note that default service procured through the competitive wholesale market likely will continue to play a central role in ensuring that electric service is available at a reasonable price, at least for the near term. Id.

With the end of the transition period less than three months away, we need to review our default service supply procurement policies to ensure that smaller customers achieve the full benefits of the competitive wholesale market. Our current policies for default service pricing and supply procurement were established only 18 months ago. See D.T.E. 02-40-B. Yet, in the two years since we sought comment in that proceeding, the Department, industry participants, and customers have gained a great deal of experience in the retail and wholesale competitive markets. As we have said before, the Department will periodically review the effectiveness of our policies and modify them when circumstances warrant. Pricing and Procurement of Default Service, D.T.E. 99-60-A at 6 (2000). The Department now seeks comment from all interested persons on how our current default service procurement policies

³ Information on customer migration is available from the Division of Energy Resources at <http://www.mass.gov/doer>. July 2004 is the most recent month for which customer migration data are available.

could be modified to ensure that the benefits of the competitive market accrue to all Massachusetts ratepayers.

II. DEFAULT SERVICE POWER SUPPLY PROCUREMENT OPTIONS

The Department initially required each distribution company to procure 100 percent of its default service power supply requirements for smaller customers in a single solicitation.

D.T.E. 99-60-A at 14-16. The Department revised this policy in D.T.E. 02-40, stating that, because prices in the wholesale market can change quickly, procuring 100 percent of supply in a single solicitation could result in prices that represent an “anomalous market condition” and could lead unwanted levels of price volatility. D.T.E. 02-40-B at 45.

In terms of contract length, in D.T.E. 02-40-B the Department stated that shorter-term procurements would ensure that default service rates “more accurately reflect market prices” but at a cost of increasing the “volatility of default service prices.” Id. at 44-45. Conversely, lengthening the procurement term would provide for more price stability but would weaken the connection to market prices. Id.

In 2002, the Department revised our policy to require distribution companies to procure 50 percent of their residential and small C&I supply requirements semi-annually for twelve-month terms, stating that such an approach is a better balance “between price certainty and price efficiency.” Id. As a result, each distribution company’s default service supply for a particular six-month term is provided by a portfolio of resources from the company’s two most recent supply solicitations, with default service prices calculated based on the winning bids of those solicitations.

Some jurisdictions (e.g., Connecticut, Maine, New Jersey) employ a more segmented portfolio approach to procure default service supply. Sometimes referred to as a “laddered approach,” a portfolio of several shorter and longer term contracts is procured for overlapping terms. An example of such a laddered approach would be one in which supply is procured annually, with one-third of the supply requirement procured for a one-year term, one-third of the requirement procured for a two-year term, and one-third of the requirement procured for a three-year term. An even more segmented portfolio approach was offered for Department consideration in D.T.E. 02-40. In this proposed approach, each distribution company would use eight quarterly solicitations to procure its default service supply requirement. Id. at 41. Each company’s default service rates would change quarterly and would be based on the winning bids of the eight solicitations from which supply was procured for that quarter.⁴ Id.

In this proceeding, the Department seeks comments regarding the advantages and disadvantages associated with increasing the number of solicitations used to procure default service supply. The Department wants to learn whether an increased number of solicitations would benefit smaller customers. In addition, the Department seeks comments regarding the advantages and disadvantages of changing the length of the default service supply procurement term as part of an overall portfolio approach to procuring default service supply.

Finally, Massachusetts uses competitive solicitations, through distribution company-issued requests for proposals, to procure default service supply. By way of contrast, Maine

⁴ The Department declined to adopt this approach at the time out of concern that it would be too complex and burdensome to implement. D.T.E. 02-40, at 45.

and New Jersey use statewide solicitations to procure default service supply (with New Jersey using a descending clock auction process).⁵ In this proceeding, the Department seeks comments regarding the advantages and disadvantages of a statewide procurement process for default service load.

III. REQUEST FOR COMMENTS

The Department requests comments on the issues discussed above and other procurement-related issues of interest.⁶ In addition to answering the specific questions below, the Department invites commenters to submit proposals regarding the number of solicitations that, in conjunction with procurement terms and the manner of procurement, will best ensure that smaller customers receive benefits (e.g., a portfolio approach). For any specific proposals addressed in your comments, please discuss whether the Department currently has the statutory authority for implementation or whether specific statutory changes must be considered.

1. Would smaller customers be better served if power supply for default service is procured using a portfolio of more than two solicitations? Please discuss the advantages and disadvantages of increasing the number of solicitations used to procure default service supply.

⁵ Basic generation service in New Jersey and standard offer service in Maine are comparable to default service in Massachusetts.

⁶ Because the costs to be included in default service rates are currently the subject of another proceeding, this issue should not be addressed here. See Default Service Costs, D.T.E. 03-88 (2003).

2. Would smaller customers be better served if power supply for default service was procured for a term longer than twelve months? Please discuss the advantages and disadvantages of using supply terms greater than twelve months. In particular, please discuss:
 - a. whether longer contract terms are likely to produce lower prices,
 - b. how such an approach would affect price certainty and market efficiency, and
 - c. how such an approach could be tailored to accommodate customer migration to competitive supply.
3. Would smaller customers be better served if power supply for default service was procured on a statewide basis? Please discuss the advantages and disadvantages of using a statewide approach to default service procurement.
4. Would smaller customers be better served if power supply for default service was procured using an auction process (e.g., descending clock) rather than through requests for proposals? Please discuss the advantages and disadvantages of using an auction process to procure default service. In particular, please discuss whether using an auction is likely to produce lower default service prices.
5. Although the term “default service” is statutory, G.L. c. 164, § 1, it has confused some customers because of its unintended suggestion of nonfeasance in performing a legal or contractual obligation. Is there some better or more descriptive term that ought to be used by the distribution companies on and after March 2005?

Initial comments should be submitted to the Department by January 10, 2004. Any responsive comments should be submitted by January 24, 2004. One original and ten copies of all comments should be filed with Mary Cottrell, Secretary of the Department referencing docket number D.T.E. 04-115. All comments exceeding ten pages in length (double spaced) must be accompanied by an executive summary of no more than two pages, double-spaced. Comments should be submitted to the Department in hard copy and electronic format using one

of the following methods: (1) by e-mail attachment to dte.efiling@state.ma.us or (2) on a 3.5" disk, IBM-compatible format. Comments submitted in electronic format will be posted on the Department's Website, <http://www.mass.gov/dte>.

By Order of the Department,

/s/

Paul G. Afonso, Chairman

/s/

James Connelly, Commissioner

/s/

W. Robert Keating, Commissioner

/s/

Eugene J. Sullivan, Jr., Commissioner

/s/

Deirdre K. Manning, Commissioner